

Internal Revenue Service

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PLR-152822-08

Date:

April 16, 2009

Entity:

State:

Authority:

Members:

Dear _____ :

This letter responds to a letter from your authorized representative dated November 24, 2008, as well as subsequent correspondence, submitted on behalf of Entity, requesting rulings that Entity's income from certain activities is excludable from gross income under § 115(1) of the Internal Revenue Code (the Code), and that Entity is excused from the requirement of § 6033 of the Code to file an annual information return.

FACTS

Entity is a nonprofit corporation formed under the laws of State as part of a telecommunications project of the Authority. Both Entity and Authority are organizations described in § 501(c)(3), whose members are political subdivisions of State.

Entity is controlled by its board of directors, comprised of representatives of its members (current members are listed above in the legend of this letter). Each member of Entity must be a state, a political subdivision of a state, or an entity the income of which is excluded from gross income under § 115(1).

Entity was created to deliver affordable broadband connectivity to largely rural areas. Its core objectives are to enhance educational proficiency, stimulate economic development, and create a reliable network delivery system for Entity's members.

Entity leases equipment and facilities from Authority to operate a telecommunications system on behalf of its members. Entity provides internet and data transmission services, fiber leasing, and network management and consulting to its members and other State municipalities, enabling them to communicate more effectively and efficiently. It maintains a fully staffed operations center to monitor and manage its equipment and services.

Entity represents that it is not a party to any joint venture or partnership with any person or entity whose income is not excluded from gross income by § 115.

Entity receives fees for the services it provides, with the vast majority of this revenue coming from municipalities, colleges, rural libraries, hospitals, and other governmental organizations.

Entity's bylaws provide that the board of directors, after retaining a reasonable amount of Entity's income to ensure adequate cash reserves, shall distribute such income to Entity's members. Entity's articles of incorporation provide that upon dissolution, and after payment of all of Entity's liabilities, the board of directors shall distribute Entity's assets to a state or the political subdivisions of a state for a public purpose. Any assets not so distributed by the board shall be distributed by a court of competent jurisdiction on the same basis.

LAW AND ANALYSIS

Section 115(1) provides that gross income does not include income derived from any public utility or the exercise of an essential governmental function and accruing to a state or a political subdivision of a state.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated that the statutory exclusion was intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of a corporation or other entity engaged in the operation of a public utility or the performance of some governmental function that accrued to either a state or municipality. The ruling stated that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and which are within the ambit of a sovereign properly to conduct. The ruling concluded that because the participating political subdivisions have an unrestricted right to receive in their own right their proportionate share of the investment fund's income as it is earned, the fund's income accrues to them within the meaning of § 115(1).

In Rev. Rul. 90-74, 1990-2 C.B. 34, the Service determined that the income of an organization formed, funded, and operated by political subdivisions to pool various risks arising from their obligations regarding public liability, workers' compensation, or employees' health is excludable from gross income under § 115. In this ruling, private interests did not materially participate in the organization, nor did they benefit more than incidentally from the organization.

Section 6033(a)(1) provides in general that every organization exempt from taxation under § 501(a) shall file an annual informational return. Section 6033(a)(3)(B)

provides in general that the Service may relieve an organization from filing the return required by § 6033(a)(1) if it determines that such a filing is not necessary to the efficient administration of the internal revenue laws.

Under the authority of § 6033(a)(3)(B), § 3.01 of Rev. Proc. 95-48, 1995-2 C.B. 418, provides that an organization that is either a governmental unit or an affiliate of a government unit is not required to file Form 990, Return of Organization Exempt from Income Tax. Section 4.02 of Rev. Proc. 95-48 provides that an organization is treated as an affiliate of a government unit if it is described in § 501(c), and its income, derived from activities constituting the basis for its exemption under § 501(c), is excluded from gross income under § 115.

Entity, on behalf of its members, provides telecommunications services to mostly rural areas of State. Entity is the means by which its members can pool resources to achieve a level of communications services no single city or county could afford to provide on its own. Providing telecommunications services to and for its members and other municipalities constitutes the performance of an essential government function within the meaning of § 115(1). See Rev. Rul. 90-74 and Rev. Rul. 77-261.

Entity's current income accrues to its members, all of which are political subdivisions or entities the income of which is excluded from gross income under § 115(1). No private interests materially participate in the operation of, or otherwise benefit more than incidentally from, Entity. Upon dissolution, Entity's assets will be distributed to a state or to political subdivisions of a state for a public purpose. See Rev. Rul. 90-74.

Based solely on the facts and representations submitted by the Entity, we conclude that—

- (1) as of the date the amendments are adopted, the income of Entity is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof for purposes of § 115(1), and
- (2) Entity is an affiliate of a governmental unit within the meaning of § 4.02 of Rev. Proc. 95-48.

Consequently, we hold that—

- (1) Entity's income is excludable from gross income under § 115(1), and
- (2) Entity is not required to file Form 990.

Except for the specific rulings above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the

Code. Specifically, we express or imply no opinion as to whether Entity has unrelated business taxable income under § 512 and must file a Form 990-T, Exempt Organization Business Income Tax Return.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

SYLVIA HUNT
Assistant Chief
Exempt Organizations Branch 2
Office of Division Counsel /
Associate Chief Counsel
(Tax Exempt & Government Entities)

enclosure: copy for § 6110 purposes

cc: